DA 97-1609

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
1997 Annual Access	)	
Tariff Filings	)	CC Docket No. 97-149
	)	

ORDER DESIGNATING ISSUES FOR INVESTIGATION
MEMORANDUM OPINION AND ORDER ON RECONSIDERATION

Adopted: July 28, 1997 Released: July 28, 1997

By the Deputy Chief, Common Carrier Bureau:

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Paragraph Nos.

I. INTRODUCTION

1. On June 27, 1997, we released the *1997 Annual Access Order*, which, *inter alia,* suspended for one day the annual access tariffs filed by several incumbent local exchange carriers, imposed an accounting order, and initiated an investigation into the lawfulness of a number of issues raised by these tariff filings.[1] We concluded that the annual access tariffs filed by 15 price cap LECs raised significant questions of lawfulness that warranted investigation.[2] We also concluded that provisions in the annual access tariffs filed by the Puerto Rico Telephone Company (PRTC) and a number of other smaller rate-of-return carriers raised questions of lawfulness that warranted investigation[3]

2. In this Order, we designate for investigation issues regarding common line costs for all 15 price cap carrier, equal access exogenous cost changes for 13 carriers, and other billing and collection expenses for four price cap carriers. We also designate for investigation issues regarding cash working capital for four rate of return carriers. In addition, on our own motion, we reconsider our decisions to suspend and investigate price cap LECs' growth factor calculation issues, two price cap LECs' equal access exogenous cost expense issues, all rate of return LECs' non-recurring charge (NRCs) issues, and cash working capital issues for four rate-of-return companies.

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[1] 1997 Annual Access Tariff Filings, National Exchange Carrier Association Universal Service Fund and Lifeline Assistance Rates, Transmittal No. 759, CC Docket No. 97-149, Memorandum Opinion and Order, DA 97-1350 (Com. Car. Bur., rel. June 27, 1997) (*1997 Annual Access Suspension Order).*

[2] Those carriers were: Ameritech Operating Companies (Ameritech), Bell Atlantic Telephone Companies (Bell Atlantic), BellSouth Telecommunications, Inc. (BellSouth), Frontier Communications of Minnesota and Frontier Communications of Iowa (Frontier), GTE System Telephone Companies (GSTC), GTE Telephone Operating Companies (GTOC), Aliant Communications. Co. (Aliant), Nevada Bell (Nevada), New York Telephone and New England Telephone and Telegraph Company, (collectively NYNEX), Pacific Bell (Pacific), Rochester Telephone Corporation (Rochester), Southern New England Telephone Company (SNET), Southwestern Bell Telephone Company (SWBT), Sprint Local Telephone Companies (Sprint), and U S WEST Communications (U S WEST).

[3] Those other companies were: Chillicothe Telephone Company (Chillicothe), Concord Telephone Company (Concord), Horry Telephone Company (Horry), Virgin Island Telephone Company (Virgin Island), Rock Hill Telephone Company (Rock Hill), Home Telephone Company (Home), Fort Mill Telephone Company (Fort Mill), Lancaster Telephone Company (Lancaster), Lufkin-Conroe Telephone Company (Lufkin-Conroe), Buffalo Valley Telephone Company (Buffalo Valley), El Paso Telephone Company (El Paso), Harrisonville Telephone Company (Harrisonville), Wabash Telephone Company (Wabash), Mt Horeb Telephone Company (Mt. Horeb), Roseville Telephone Company (Roseville), and Union Telephone Company (Union).

II. PRICE CAP CARRIERS

A. Common Line Issues

1. Background

3. For price cap LECs, the maximum end user common line (EUCL) and carrier common line (CCL) rates are set in accordance with the various requirements contained in Parts 61 and 69 of the Commission's rules. A key element in these requirements is the base factor portion (BFP) revenue requirement, which is defined in Part 69 as that portion of an incumbent LEC's common line revenue requirement that remains after the assignment of certain specified common line investment and expenses exclusively to the CCL element.[4] Section 69.502 provides that projected EUCL revenues should be deducted from BFP, with the remainder being assigned to the CCL element.[5]

4. Under our access charge and price cap rules, each incumbent LEC subject to price cap regulation projects its BFP revenue requirement and its EUCL demand in order to determine the maximum CCL charge and EUCL charge,[6] subject to the common line basket's price cap.[7] More specifically, our rules require an incumbent LEC to divide its projected BFP revenue requirement for the upcoming access year by its projected EUCL demand to determine its prospective interstate per-line common line revenue requirement.[8] An incumbent LEC then recovers these costs in part through the EUCL charge, up to a cap of

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[4] Costs assigned directly to the CCL element and, therefore, recovered solely from IXCs, are those attributable to customer premises equipment (CPE), surrogate CPE, and customer premises wiring included in information origination-termination equipment accounts. 47 C.F.R. §§ 69.2(r), 69.501(b)-(c). The Commission recently revised section 69.501 to include the costs of public telephone loops in the BFP. *See* Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, Report and Order, 11 FCC Rcd. 2054 (996); Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Order on Reconsideration, 11 FCC Rcd 21233 (1996) (*Payphone Reconsideration Order*).

[5] Section 69.502 also provides that projected Special Access surcharges shall be deducted from the BFP. 47 C.F.R. § 69.502.

[6] EUCL charge is also referred to as the subscriber line charge (SLC).

[7] After January 1, 1998, incumbent LECs will also use their projected BFP revenue requirement in developing the residual presubscribed interexchange carrier charge (PICC). *See* Access Charge Reform, CC Docket No. 96-262, First Report and Order, FCC 97-158 at ¶¶ 94-104 (rel. May 16, 1997) (*Access Charge Reform Order*).

[8] *See* 47 C.F.R. §69.104.

$3.50 for residential and single-line business (SLB) lines,[9] or $9.00 for multi-line business (MLB) lines.[10] Until January 1, 1998, an incumbent LEC recovers its remaining common line costs through the per-minute CCL charge. A price cap LEC then determines its maximum per-minute CCL charge pursuant to the formula prescribed in Section 61.46(d), which factors in the proposed EUCL charge set above.[11]

5. As discussed in the *1997 Annual Access Suspension Order*, the recent increase in the MLB EUCL charge cap increased the impact that per-line BFP revenue requirement projections have on EUCL charges, maximum CCL charges, and the total amount of common line revenues that a price cap LEC reasonably can expect to recover.[12] When a price cap carrier's per-line BFP revenue requirement projection is greater than the $3.50 residential/SLB EUCL cap but does not exceed the $9.00 MLB EUCL cap, that projection will effectively determine the relative proportions of its common line revenue recovered from end users, via EUCL charges, and interexchange carriers, via CCL charges. A relatively lower projected per-line BFP revenue requirement generally will lead to a relatively lower MLB EUCL charge and an increase in the maximum CCL charge. Because, under price cap regulation, total common line revenues are constrained by the relevant price cap formulas rather than a projected revenue requirement, a LEC's total anticipated common line revenues would not necessarily decrease with a lower projected per-line BFP projection. Rather, under those formulas, so long as this year's growth in minutes of use per common line is expected to exceed half the previous year's growth, the price cap LEC would expect to receive greater total common line revenues by charging relatively lower EUCLs and relatively higher CCL charges.[13]

6. In the *1997 Annual Access Suspension Order*, we suspended the portions of the price cap LECs' tariffs relating to the BFP revenue requirement and EUCL demand forecasts for one day and set these tariff provisions for investigation.[14] In its petition requesting that the Commission suspend and investigate the price cap LECs' tariff revisions, AT&T provided

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[9] 47 C.F.R. § 69.152(d)(1). Effective January 1, 1998, the EUCL charge cap on second and additional residential lines will increase to $5.00. 47 C.F.R. § 69.152(d)(2).

[10] 47 C.F.R. § 69.152(b)(3).

[11] 47 C.F.R. § 61.46(d).

[12] *1997 Annual Access Suspension Order* at ¶ 5.

[13] This outcome results from the Commission's decision in the Price Cap Proceeding to adopt the "balanced 50-50" formula that reduces the maximum CCL charge by a percentage representing half the growth in minutes of use per line in the prior year (g/2). 47 C.F.R. § 61.46(d). *See also* Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, 5 FCC Rcd 6786, 6793-95 (1988).

[14] *1997 Annual Access Suspension Order* at ¶ 22.

its own estimates of the BOCs' BFP revenue requirements, using historical trend data.[15] We stated in the *1997 Annual Access Suspension Order* that we were not persuaded that AT&T's estimates had sufficiently accounted for changes in the treatment of general support facilities (GSF) investment and expense and other regulatory changes that would affect apparent historical patterns. Nevertheless, we found that the issues raised by the petitions raised substantial questions of lawfulness that warranted investigation of all price cap LECs' BFP forecasts, in light of the failure of the price cap LECs to offer complete support for their projected BFP revenue requirements and in light of the wide disparity between the projections of all of the BOCs and the projections offered by AT&T in its petition.[16]

a. Projected BFP Revenue Requirement

7. Several price cap carriers used historical trends to develop their forecasts of BFP revenue requirements for the 1997-98 tariff year.[17] Bell Atlantic, for example, assumed that the expected cost growth rate would follow the historical 1995 to 1996 pattern, and uses the growth in costs for this period to estimate costs for the 1997-98 tariff year.[18] Similarly, NYNEX states that it developed an 18-month normalized, subject-to-separations (STS) growth rate using 11 months of data from 1995 and 1996 to project its BFP revenue requirement.[19] These carriers then adjust their revenue requirement forecasts to account for changes in various Commission rules, income tax adjustments, and other exogenous cost factors.

8. Other carriers state that they developed projections based on a model or using a "bottoms-up approach."[20] Pacific Bell, for example, claims that, to calculate its BFP revenue

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[15] AT&T Petition at 2-5 and Appendix B.

[16] *1997 Annual Access Suspension Order* at ¶ 22.

[17] *See, e.g.*, Bell Atlantic Telephone Companies, 1997 Annual Price Cap Filing, Trans. No. 970, Volume 1-1, Supporting Documentation, Description and Justification (filed June 16, 1997) (Bell Atlantic 1997 Access Filing), at pages 3-1 to 3-7; NYNEX Telephone Companies, 1997 Annual Access Charge Tariff Filing, Trans. No. 455, Volume 1, Description and Justification (filed June 16, 1997) (NYNEX 1997 Access Filing), at pages 8-13; U S WEST Communications, 1997 Annual Access Tariff Charge Filings, Trans. No. 847, Volume 1, Description and Justification (filed June 16, 1997) (U S WEST 1997 Access Filing), at pages 4-10 to 4-14.

[18] Bell Atlantic 1997 Access Filing, Description and Justification at 3-1 to 3-7.

[19] NYNEX 1997 Access Filing, Description and Justification at 8-13.

[20] *See, e.g.*, Pacific Bell, 1997 Price Annual Access Charge Tariff Filing, Transmittal No. 1921, Volume 1-1, PCI Revisions (filed June 16, 1997) (Pacific Bell 1997 Access Filing), at pages 16-20; Southwestern Bell Telephone, 1997 Annual Access Tariff Charge Filing, Trans. No. 2640, Volume 1 (filed June 16, 1997) (SWBT 1997 Access Filing), at page 5-3.

requirement for the 1997-98 tariff year, it started with its total company budget based on Part 32 of the Commission's rules.[21] Pacific Bell then states that, after analyzing its operating environment, "economic and demographic forecasts were developed based on that analysis."[22] Pacific Bell states that its forecasted BFP revenue requirement for the 1997-98 tariff year, calculated using this "bottoms-up" approach, represents a 1.57 percent increase over calendar year 1996, after adjustment for the changes to the BFP calculation process required by the *RAO 20 Order*[23] and the *Payphone Reconsideration Order*.[24] SWBT indicates that it developed projected BFP revenue requirement for the 1997-98 tariff year by using "its Interstate Cost Analysis System to calculate the Common Line -- BFP costs." SWBT states that "[t]his model conforms with cost allocation requirements contained in parts 36 (Jurisdictional Separations) and 69 (Access Charges) [of the Commission's rules.]"[25]

9. Several other price cap carriers give little or no documentation as to how they develop their BFP revenue requirement projections. Ameritech, for instance, states that it developed its BFP estimates "on a study area basis in accordance with Price Cap rules."[26] Ameritech also states that it estimated prospective end-user demand for the 1997-98 tariff year "based on historical growth patterns."[27] BellSouth simply reports its projected BFP revenue requirement without any explanation of the basis for its projection.

10. After the effectiveness of its annual access tariffs, Bell Atlantic submitted calculations of its actual BFP revenue requirements for 1991-1996.[28] In addition, Bell Atlantic submitted adjustments that must be made to its revenue requirements to reflect changes in several of the Commission's rules.[29] Specifically, Bell Atlantic adjusted its 1991 and 1992 actual interstate BFP revenue requirements for changes in the SPF, and its 1991 to

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[21] 47 C.F.R. Part 32. *See* Pacific Bell 1997 Access Filing at pages 16-20.

[22] Pacific Bell 1997 Access Filing at page 17.

[23] Responsible Accounting Officer Letter 20, Uniform Accounting for Postretirement Benefits Other than Pensions in Part 32, Report and Order, 12 FCC Rcd 2321 (1997) (*RAO 20 Order*).

[24] 11 FCC Rcd 21233.

[25] SWBT 1997 Access Filing at page 5-3.

[26] Ameritech Operating Companies, 1997 Annual Access Tariff Charges, Trans. No. 1106, Volume 1-2 (filed June 16, 1997) (Ameritech 1997 Access Filing), at page 8.

[27] *Id.* at 7.

[28] Letter from Joseph J. Mulieri, Director, Government Relations -- FCC, to Brad Wimmer, Economist, Competitive Pricing Division, filed July 18, 1997.

[29] *Id.*

1993 BFP revenue requirements for changes in the allocation of GSF.[30] Using these adjusted BFP revenue requirements, Bell Atlantic calculated the year-to-year percentage increase in BFP revenue requirements.[31] The year-to-year percentage increase in Bell Atlantic's adjusted BFP revenue requirements ranged from 9.22 to 2.45 percent and had a median of 4.38 percent.[32] Using the year-to-year percentage changes, Bell Atlantic performed a simple time-trend analysis and estimated its percentage increase in its BFP revenue requirement for the 1997-98 tariff year.[33] This analysis resulted in a predicted percent increase in BFP revenue requirement of 1.46 percent between calendar years 1996 and 1997.[34] By contrast, Bell Atlantic shows that the BFP revenue requirement in its 1997-98 tariff filing is 3.3 percent (annualized) higher than its actual 1996 BFP revenue requirement.[35]

11. Sprint provides calculations of its actual BFP revenue requirement for 1993-1996, noting that data prior to 1993 should not be used in its trending process because these data reflect information from before the GSF restructure. Sprint shows that the BFP revenue requirement it filed for the 1997-98 tariff year exceeds a projection using revenue requirements from 1993-1996 and AT&T's methodology by over $8 million.[36]

b. Projected End-User Demand

12. The majority of price cap carriers indicate that they evaluated a variety of factors, such as the economic performance in a study area and demographic factors, to estimate end-user demand. For example, NYNEX states that it obtained historical demand data, by class of service, for the following categories: (1) Residence (excluding Lifeline); (2) Lifeline; (3) Single Line Business; and (4) Multi-line Business and Centrex. NYNEX then states that it projected the growth in access lines for each state and subscriber category using forecasts of economic growth, non-farm employment, population, unemployment, real personal income, interest rates, housing starts, and competitive pressures. NYNEX, however, does not provide any information quantifying these factors or explaining how they were weighed. It states that its 1996 forecast of end user demand for the 1996-97 tariff year using the same method was within 0.04 percent of actual EUCL demand. Pacific Bell states that it used information on "market intelligence, historic demand levels, product cross elasticities,

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[30] *Id.*

[31] *Id.*

[32] *Id.*

[33] *Id.*

[34] *Id.*

[35] *Id.*

[36] Sprint Reply at Exhibit 1.

and new product introductions" to forecast EUCL demand for the Multi-line Business, Single-line Business, Centrex in service prior to July 27, 1983, Centrex in service after July 27, 1983, Residence without Lifeline, and Lifeline service classes.[37] No carrier, however, provided any specific explanation of the basis for its estimate, reporting only the results of its studies.

2. Information Requirements and Issues Designated for Investigation

13. Based on a review of the record, we concluded in the *Suspension Order* that investigation of the price cap LECs' BFP revenue requirement and EUCL demand forecasts is warranted. We here designate for investigation the issue of whether the price cap LECs have justified these projections, and direct the price cap LECs to justify their projections, and specifically to respond to the information requirements below. In this investigation, the price cap LECs have the burden of proving that their BFP revenue requirement projections and EUCL demand forecasts are just and reasonable.

14. Although our rules do not prescribe any particular methodology that incumbent LEC must use to develop their BFP revenue requirement and EUCL demand forecasts, the accuracy of LEC common line cost forecasts has often been at issue, particularly when those forecasts have departed from the trend of BFP costs.[38] In an effort to facilitate resolution of such issues we stated in the *1997 TRP* that "information on the SLC calculation should be included in the annual access tariff filing,"[39] and that "the information filed should explain any forecast that deviates from the historical cost or demand trend, and significant differences between actual results and predictions produced by forecast models used in recent annual filings."[40]

15. After conducting a preliminary analysis of the price cap LECs' current projections, we find that these projections are likely, in many cases, to be inconsistent with the recent trend of actual BFP revenue requirements. Many of the price cap LECs have neither explained fully how they derived their BFP revenue requirement and end-user demand projections,[41] nor have they shown their projections to be consistent with historical patterns.

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[37] Pacific Bell 1997 Access Filing at 18-19.

[38] Material to be Filed in Support of 1997 Annual Access Tariff Filings, Tariff Review Plans, DA 97-593 (rel. Mar. 21, 1997), ¶ 8 (*1997 TRP Order*).

[39] *Id.*

[40] *Id.*

[41] In their 1997 annual access tariff filings, Bell Atlantic and Pacific Telesis provided some information on the methods they used in developing their BFP revenue requirements. Subsequent to its filing, Bell Atlantic presented, in a written ex parte presentation, an analysis of its BFP revenue requirement's historical trend. In its comments filed in response to the petitions of AT&T and MCI,

To enable us to complete an analysis of the incumbent LECs' 1997-1998 tariff year estimates of BFP revenue requirements and EUCL demand, price cap LECs must submit the information specified below in accordance with the instructions set forth in Appendix B. The price cap LECs also may submit additional information with respect to other methods of projecting BFP revenue requirements and EUCL demand.

a. BFP Revenue Requirements

16. As discussed in more detail, below, we require each price cap LEC subject to this investigation to submit: (1) its actual BFP revenue requirements, computed using ARMIS data, if available, for each calendar and tariff year between the 1991-1992 tariff and calendar years and the 1996-1997 tariff and calendar years, and projected BFP revenue requirements filed in each year's TRP for the same period; (2) a list of any change in its BFP revenue requirements caused by any revisions to the Commission's rules over this period, including an itemized quantification of the effects of these changes; and (3) documentation that explains in detail the methodology that each LEC used to compute its BFP revenue requirement projection for tariff year 1997-98.

(1) Actual and Projected BFP Revenue Requirements

17. We require each LEC that files ARMIS data to calculate its actual interstate BFP revenue requirement for calendar years 1991-1996 and associated tariff years (beginning with the 1991-1992 tariff year) using data from ARMIS report 43−01, columns k and m. The use of ARMIS ensures that the LECs' calculated actual BFP revenue requirements are easily replicable and verifiable on the basis of publicly available data. We require price cap LECs that did not file ARMIS data during this period to develop their actual BFP revenue requirements using separated, interstate data from company records.[42] We also require each price cap LEC to submit its projected BFP revenue requirements filed in each year's TRP since tariff year 1991-92. With this information, we intend to establish the historical pattern of the LECs' BFP revenue requirements and the accuracy of their past projections. LECs are, therefore, required to explain fully any significant differences between each annual BFP revenue requirement projection and the LEC's actual BFP revenue requirement.[43] For purposes of this

Sprint also provided some explanation of its projections. Sprint Comments, filed June 26, 1997, Exhibit 1.

[42] See Appendix B for instructions on how these revenue requirements shall be calculated.

[43] We do not require LECs to adjust this data for any changes in Commission rules that affect its BFP revenue requirement unless the change occurred during the tariff year for which its BFP revenue requirement was being projected. If a change in Commission rules occurred during the tariff year, LECs should calculate the effect such a change had on its BFP revenue requirement for that year, and include this information in its explanation of why its projection was not realized.

request, a difference will be classified as significant by comparing the projected year-to-year percentage change in BFP revenue requirements with the actual year-to-year percentage change. A difference will be considered significant if the projected percentage change is greater than or less than 10 percent of the percentage change actually realized. For example, if a LEC's BFP revenue requirement actually increases by 3 percent, and the LEC projects that its BFP revenue requirement will grow by more than 3.3 percent or less than 2.7 percent, we will classify these projections as significantly different. Additionally, LECs are required to explain fully any patterns of significant and consistent over- or under-estimation of their BFP revenue requirements that may emerge.

18. We require that actual BFP revenue requirements be calculated for calendar years 1991-1996 because LECs typically use calendar-year data to project their revenue requirements. We also require LECs to calculate actual BFP revenue requirements for tariff years 1991-1996 because to enable us to compare those data with the projected revenue requirements that the price cap LECs submitted with their annual access tariff filings for the relevant years in support of their proposed EUCL and CCL rates.[44] We intend to use calendar year BFP revenue requirements to develop historical trends of BFP revenue requirements, and use actual and projected BFP revenue requirements calculated for tariff years to determine the accuracy of LECs' past projections of BFP revenue requirements. LECs must file data on a total company basis,[45] but are free to file additional data on a study-area basis.

(2) Adjusted BFP Revenue Requirements

19. We also require LECs to provide adjusted BFP revenue requirement data for calendar years 1991-1996 in order to explain differences in LECs' actual BFP revenue requirements between calendar years 1991-1996. Accordingly, we require price cap LECs subject to this investigation to develop calendar year BFP revenue requirement series that are adjusted for the effect that changes in Commission rules had on actual BFP revenue requirements. As explained in more detail below, in fulfilling this requirement, each price cap LEC must submit an itemized list of each change in Commission rules that affected BFP revenue requirements, including (a) the date each change became effective and its impact on the BFP revenue requirement for the calendar year in which the changed rule became effective, measured in dollars; and (b) the LEC's actual BFP revenue requirements, adjusted for all such changes in Commission rules for calendar years 1991-96, reported in two series as described below.

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[44] We understand that LECs will have to use company data to calculate their actual BFP revenue requirement for tariff year 1996 (July 1, 1996 through June 30, 1997) because ARMIS data are only reported on a calendar-year basis for 1996.

[45] We project those LECs that have not filed tariffs on a holding company basis for this entire period to recast their projections on a holding company basis and for submission in this filing. These companies to explain and document fully the data, assumptions and methodologies used to derive these projections.

20. For each change in the Commission's rules that became effective on or before December 31, 1996, and that affected the LEC's BFP revenue requirement, we require each LEC to identify the change, state its effective date, and calculate the effect, in dollars, that the change had on its BFP revenue requirement. We also require the LEC to calculate the effect that each rule change would have had on BFP revenue requirements in previous years, back to 1991, had the revised rule then been in effect. For example, effective July 1, 1993, the Commission revised the rules governing the LECs' allocation of interstate costs associated with General Support Facilities (GSF). This change in rules increased costs allocated to BFP, and thus increased BFP revenue requirements. In order to compare BFP revenue requirements over the years, we require LECs to calculate the impact the change in allocation of GSF costs would have had on BFP revenue requirements in 1991, 1992, and the first half of 1993, if the revised rule had been in effect during those years. For changes that became effective after December 31, 1996, LECs must submit data that show the effect, in dollars, that these changes had on projected BFP revenue requirements prepared for their annual access tariff revisions filed to become effective July 1, 1997.

21. These lists itemizing the effect changes in Commission rules had on BFP revenue requirements shall include, *but need not be limited to*: (1) changes with respect to the treatment of GSF; (2) the phase-in of the subscriber plant factor (SPF) and dial equipment minutes of use (DEM) separations rule changes; and (3) changes to the treatment of Account 4310 of the Uniform System of Accounts, Other Long Term Liabilities, especially with respect to Other Postretirement Employee Benefits (OPEBs).

22. After determining the effect that changes in the Commission's rules had on their BFP revenue requirements, LECs must report the calculation of their adjusted BFP revenue requirements for the calendar years 1991-1996 in two series as follows. The first series must be adjusted for (1) changes to the allocation of GSF expenses; (2) the phase-in of the SPF and DEM separations allocation rule changes; and (3) revision of the allocation of Other Billing and Collection expenses to reflect a five percent allocation to the common line revenue requirement, if the LEC has not consistently allocated five percent of these expenses to the common line revenue requirement in the past. The second series must be adjusted for all changes to the Commission's rules identified above. These series must be constructed to allow for year-to-year comparisons of BFP revenue requirements. These BFP revenue requirements must be calculated in a manner consistent with the Commission's rules on December 31, 1996.

23. We intend to use these data to compare BFP revenue requirements in a consistent manner on a year-to-year basis. In their submissions, LECs must file all data underlying their computed revenue requirements, and must fully explain the data assumptions and methodology used to compute the BFP revenue requirement and projections and to adjust the revenue requirements for changes in Commission rules. This documentation shall include

an explanation of all calculations, including a list of all equations used,[46] and an explanation of the methodology used to compute the actual revenue requirements.

24. We also require these LECs to explain in detail any relatively "large" year-to-year changes that emerge in each adjusted series of actual BFP revenue requirements. Because price cap LECs will be providing only six data points, each data point will have a relatively great impact on calculation of historical trends. For each series, therefore, we intend to discount or exclude observations that we consider to be "large" deviations from the overall trend in BFP revenue requirements, absent clear evidence that such a "large" change is not an isolated occurrence, but instead represents a change in the BFP revenue requirement trend that is likely to continue over time. For example, three of the data points percent changes in Bell Atlantic's adjusted BFP revenue requirements are clustered around 4.5 percent (4.26 to 4.90 percent), and two other data points, upon visual inspection, appear to be outliers (9.22 and 2.45 percent).[47] Because of the small number of observations, excluding either of these suspected outliers from the regression analysis greatly affects Bell Atlantic's forecast. We, therefore, require each LEC to identify actual BFP revenue requirements that appear to be outliers, and furnish an explanation for the deviations. At a minimum, LECs are required to justify inclusion of BFP revenue requirements that are associated with the highest and the lowest percentage changes in BFP revenue requirements for the 1991-1996 period by showing that these results reflect a change in the BFP revenue requirement trend that is likely to continue over time. If, on the other hand, a particular percentage change is the result of a one-time event or other isolated occurrence, the LECs must explain the event and its impact, and calculate their BFP revenue requirements excluding the effects of the event.

25. The small number of observations for each LEC makes a simple trend analysis ineffective when the data used for this analysis reflect one-time events. We therefore seek information on alternative methods to forecast BFP revenue requirements. For example, we could include all LECs' BFP revenue requirements from 1991-1996 in the analysis by pooling these BFP revenue requirements into a single data set. We could then determine the average trend in the industry, or identify changes in BFP revenue requirements that are outliers. By pooling the data, we would increase the number of observations, making statistical methods more reliable. Alternatively, we could examine each LEC individually and use either the average percentage change or the median percentage change to forecast its BFP revenue requirement. We seek comment on these methodologies and on any possible alternative methods to forecast BFP revenue requirements.

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[46] Submission of a spreadsheet, where the equations are found by examining the formula used in individual cells, will not fulfill this requirement. A listing of all equations used to calculate revenue requirements and to adjust data for changes in our rules, either separately, or within a spreadsheet that has equations displayed clearly in row or column headings, for example, will fulfill this requirement.

[47] Letter from Joseph J. Mulieri, Director, Government Relations -- FCC, to Brad Wimmer, Economist, Competitive Pricing Division, filed July 18, 1997.

(3) Justification of 1997 BFP Revenue Requirement

26. All price cap LECs must explain and document fully the data, assumptions, and methodology used to derive BFP revenue requirement projections contained in the price cap LEC's access tariff revisions filed to become effective July 1, 1997. Each price cap LEC must also explain whether its projection is consistent with the historical pattern. If the LEC believes that its projection is consistent with the historical pattern, it must explain in detail this conclusion and its basis. If a LEC projection is not consistent with the historical trend, the LEC must fully explain its reasons for the deviation from the historical pattern. All worksheets used to derive projections for the 1997-98 tariff year should be filed both electronically, in a format compatible with EXCEL 4.0, and as a hard copy. Supporting worksheets must include an explanation of all calculations, including a list of all equations used.[48]

27. Additionally, for the 1997-1998 tariff year, each price cap LEC shall show separately the adjustments for the recent *OB&C Order*[49] and the *Payphone Reconsideration Order*,[50] that were reflected in its recent BFP revenue requirement projections. This showing must include a complete explanation and full documentation of the data, assumptions, and methodology used to derive these adjustments. Finally, each price cap LEC shall indicate whether it has followed the same methodology to derive its BFP revenue requirement for each year between 1991 and 1997, and, if not, must (1) explain why it changed methodologies in each case; (2) provide complete explanations of the ways in which any previous methodologies differ from the methodology used in preparing the BFP revenue requirement projection for the 1997 annual access tariff filing; and (3) explain the effect these changes had on their projections for the 1997-98 tariff year.

28. In developing their BFP revenue requirement projections, carriers in general used one of two basic methodologies. One group states that they based their projections on the historical trends of costs.[51] These carriers should be able to use the data filed in response

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[48] As noted above, submission of a spreadsheet, where the equations are found by examining the formulae used in individual cells, will not fulfill this requirement. A listing of all equations used, such as in a spreadsheet with equations displayed clearly in row or column headings, will fulfill this requirement.

[49] Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, Report and Order, 12 FCC Rcd 2679 (*OB&C Order*).

[50] 11 FCC Rcd at 2733.

[51] For example, Bell Atlantic used the percentage change in unseparated costs from calendar year 1995 to 1996 to estimate its BFP revenue requirement for tariff year 1997. While Bell Atlantic provided the worksheets showing its calculation, it did not include a complete explanation of its calculations. Bell Atlantic used the percentage change in unseparated operating expenses, total plant in service, and total reserves from calendar year 1995 to 1996 to estimate the BFP revenue requirement

to the information requirements in subsections b(1) through b(3) above. to establish the historical pattern of actual BFP revenue requirements to justify their BFP projection filed for the 1997-98 tariff year. We question the use of unseparated company data by some of these price cap LECs to calculate the percentage change in costs for projecting the company's BFP revenue requirement. Under our rules, a LEC's BFP revenue requirement is an interstate allocated cost, and its projection should, therefore, take into account the effect regulatory rules, such as separations, have on revenue requirements. We therefore require in Section II.A.2.a(1), above, that the price cap LECs provide BFP revenue requirement data using separated, interstate data from ARMIS, where possible, or from company records. If a LEC believes that the use of unseparated company data would be more appropriate, it may supply BFP revenue requirement projections using such data, provided that the LEC also demonstrates with a thorough explanation containing clear evidence that such a calculation produces a result that is more accurate than that produced by the use of separated, interstate data. Such submissions must be in addition to, and not in lieu of, submissions using separated, interstate data.

29. The second group of carriers states that they estimated costs using either a "bottoms-up" approach or a model. We require that these carriers fully explain their methodology and provide us with detailed information regarding the factors underlying the projection, and the weight given to each factor. Fundamentally, a bottoms-up approach estimates the value of factors, such as total operating expenses and net investment, directly affecting BFP revenue requirements for the period of the projection. Using these values, a bottoms-up approach projects the revenue requirement based on underlying estimates of factors that directly affect BFP. Carriers that followed this approach must submit information that documents the source of their final BFP revenue requirement projections, including worksheets displaying any statistical analysis supporting their projections, and must also file any underlying estimates incorporated into the final projections. We also require these carriers to explain the basis for their conclusion that this method produces results that are at least as accurate as projections developed using historical trends.

30. If a LEC followed the same methodology for each year between 1991 and 1997, we expect to be able to replicate its past BFP revenue requirement projections using the methodology described by the LEC in response to this Order. LECs that have adjusted their methodology over time must provide the same information regarding their projection methodology for 1995-96 and 1996-97 tariff years that we require for their most recent BFP revenue requirement projections. In order to understand current projections and to compare them to previous projections, we find it necessary to be able to replicate at least two previous BFP revenue requirement projections.

b. End-User Demand

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for tariff year 1997.

31. All price cap LECs must provide the past actual average number of total billable access lines, multi-line business lines, residential and single-line business lines, for the past six tariff years (beginning with the 1991-1992 tariff years), using ARMIS data, if available, and the projections of these lines filed for each of these tariff years. If ARMIS data are not available for a particular LEC, the LEC must use company records to provide this information.[52] For periods where the difference between the actual number of lines and the projected number of lines is significant, we require LECs to explain in detail the difference between their projection and the actual number of lines. As in the case of BFP revenue requirements, we define a difference to be "significant" for this purpose if the projected percentage change is greater than 10 percent of the actual percentage change.[53]

32. Most LECs report that they use information concerning a variety of factors, such as general economic performance and demographic characteristics, to estimate end-user demand. We require each LEC that had a significant difference between its projection of lines and the actual number of lines in any tariff year (1991-1996) to identify separately for those years the variables used to forecast end-user demand, and the weight given to each variable. Additionally, each such LEC must provide information concerning, at least, the two most significant individual variables that did not change as expected and thus resulted in an inaccurate projection of end-user demand. We also require these LECs to explain whether, and why, they expect such unexpected changes to be evidence of a change in the underlying trend of end-user demand, or a one-time event that does not affect the overall trend of end-user demand. A separate explanation must be provided for each individual class of lines (*i.e.* multi-line business, single-line business, and residential) and for total lines.

33. We also require that each LEC either: (1) demonstrate that the projection for the 1997-1998 tariff year is consistent with the value predicted by the historical trend of end-user demand; or (2) state specifically the underlying factor or factors that they expect will change, and the projected effect(s) of the expected change(s), expressed in a numerical prediction. For example, if the LEC cites an expected increase in the demand for second lines, it must provide an analysis that justifies this expected demand increase. To demonstrate whether projections are consistent with historical trend, LECs must provide trend analyses using the actual number of lines and the natural logarithm of the number of lines, as reported in ARMIS, if available. These trends must be estimated separately for total billable lines, residential lines, multi-line business lines, and single-line business lines, using calendar year

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[52] LECs must calculate the "average" number of lines for any given tariff year by dividing by five the sum of the line counts from the last day of each quarter of that tariff year (September 30, December 31, March 31, and June 30) and the line count from the last date of the previous tariff year (June 30 of the previous tariff year). In addition to average line counts calculated using this quarterly method, LECs may also supply average line counts calculated by dividing by 13 the sum of their line counts for the last day of every month of the tariff year and the line count for the last day of the last month of the previous tariff year.

[53] *See supra* ¶ 17.

data from 1991-1996. We also require LECs to explain any significant differences between the projection filed in their 1997-98 Annual Access Tariffs, and the forecasts derived from the trend analysis we are requiring.[54] Those price cap LECs that are unable to demonstrate that their projections for tariff year 1997-1998 are consistent with the historical trend must also explain and document the data and methodology used to derive their EUCL demand projections filed in their 1997-1998 TRP. All worksheets used to derive these projections must be filed both electronically, in a format compatible with EXCEL 4.0, and in hard copy. As in the case of BFP revenue requirement projections, carriers are required to provide the requested information on a company-wide basis, but may, in addition, provide this on a study-area, or smaller, basis if they desire. LECs should also explicitly show the number of public payphone lines they are projecting for tariff year 1997-98. In addition, each LEC must indicate the number of semi-public payphones that, prior to the *Payphone Reconsideration Order*,[55] it charged single-line business EUCL charges, but will now charge multi-line business EUCL charges. These projections must be compared with historical counts of public and semi-public payphone lines. Additionally, LECs must explicitly show how they are treating ISDN lines in their 1997-98 projections.

c. Per-Line BFP Revenue Requirements

34. Finally, price cap LECs must file their actual and projected BFP revenue requirements on a per-line basis for each tariff year between 1991 and 1996. These revenue requirements must be calculated by dividing the actual BFP revenue requirement by total billable lines. The price cap LECs must then explain any differences between these actual per-line BFP revenue requirements and their per-line BFP revenue requirements projected in their Annual Access Tariff filing for each year.

B. Equal Access Exogenous Cost Changes

1. Background

35. In the *Access Charge Reform Order*, the Commission ordered price cap LECs to make an exogenous cost decrease to account for the December 31, 1993 completion of the amortization of equal access expenses that the Commission had required to be deferred and amortized over eight years.[56] The Commission found that these equal access expenses had been completely recovered, and directed price cap LECs to make a downward exogenous

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[54] We use the same definition for significant as defined in the case of BFP revenue requirements and comparison of past actual and projected end-user demand. See, supra ¶ 17.

[55] 11 FCC Rcd at 21323-21324.

[56] *Access Charge Reform Order* at ¶ 314. The background to the Commission's treatment of equal access costs is set forth in that decision.

adjustment to the traffic sensitive basket in their 1997 annual access tariff filing.[57] The Commission found that the removal of these equal access expenses would ensure that ratepayers are not paying for costs that have already been completely recovered.[58]

36. The price cap LECs filed with their 1997 annual access tariff filings summary support information, which explained, *inter alia*, the manner in which the carriers calculated the equal access exogenous adjustment. The majority of the LECs determined the exogenous adjustment by calculating the portion of equal access revenues at the initiation of price cap regulation that constituted the expenses subject to the special amortization. The LECs then calculated the expense amount to be removed from the traffic sensitive basket by reducing the amount of these equal access expenses by the amount of the price cap index (PCI) change in the traffic sensitive basket between the initiation of price cap regulation and June 30, 1997.[59] LECs argue that it was proper to reduce their equal access expenses subject to the amortization by the amount of the PCI change in the traffic sensitive basket between January 1, 1991 and June 30, 1997. Furthermore, the LECs argue that the equal access exogenous adjustment removes costs that do not change with demand. They state that because these costs are fixed, any adjustment for demand growth is inappropriate. In contrast to the other price cap LECs, Aliant determined the portion of equal access revenues at the initiation of price caps that constituted the equal access expenses subject to amortization ("z/R_{96}"), and then increased that amount to account for the change in total revenue for the traffic sensitive basket between the initiation of price caps and the present.[60]

37. In the *Annual Access Suspension Order*, we decided to investigate whether LECs have fully removed those equal access expenses from their rates, as required by the

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[57] *Id.* at ¶ 314. *See id.*, ¶¶ 302-314 for an extensive discussion of the amortized equal access costs.

[58] *Id.* at ¶ 302.

[59] This may be represented mathematically by the following formula:

$$(z/R_{96})*(PCI_{96}/PCI_{I})$$

where z/R_{96} represents the portion of the equal access revenues at the initiation of price caps that constituted amortized equal access costs , and PCI_{96}/PCI_{I} represents the change in the PCI from the initiation of price cap regulation to present.

[60] Specifically, Aliant's exogenous adjustment can be represented mathematically as follows:

$$(z/R_{96})*(R_{96}/R_{I})$$

where z/R_{96} represents the portion of the equal access revenues at the initiation of price caps that constituted amortized equal access costs , and R_{96}/R_{I} represents the change in total revenues for the traffic sensitive basket from the initiation of price cap regulation to present.

Access Charge Reform Order.[61] We stated that we were not convinced that the LECs had completely removed equal access exogenous cost expenses because after they calculated these expenses, they had reduced this amount by the amount of the PCI change in the traffic sensitive basket between the initiation of price cap regulation and June 30, 1997. We stated that instead of reducing this exogenous cost adjustment by changes in the PCI, LECs may need to increase the adjustment by the percentage change in base period revenue ("R") (assuming that revenues have increased) from the date each LEC made its first annual access price cap filing through June 30, 1997. We also found that the documentation of the unadjusted equal access expense provided by Ameritech and SNET indicates that they may have failed to implement properly the requirements of the *Access Charge Reform Order*. Although we noted that Aliant appears to have made the "R" adjustment to its equal access expense, we stated that we were not persuaded that Aliant's exogenous cost adjustment was correctly calculated or fully supported.

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[61] *Annual Access Suspension Order* at ¶ 36.

2. Information Requirement and Issues Designated for Investigation

38. Exogenous Cost True-Up Adjustment. In implementing the exogenous reduction required by the *Access Reform Order*, Aliant is the only price cap LEC that made an adjustment to account for revenue changes between the date that it made its first annual access price cap filing and June 30, 1997. All other LECs reduced the equal access expense subject to amortization by the percentage change in their traffic sensitive PCI between the date they made their first price cap filing and June 30, 1997.

39. AT&T recommends that the Commission require LECs to adjust their baseline amortized equal access costs for revenue growth that has occurred since January 1, 1991. AT&T suggests that the Commission require LECs to apply the "R" value true-up in order to calculate the exogenous cost adjustments that must be made effective July 1, 1997.[62] According to AT&T, this "R" value true-up would adjust the price cap LECs' amortized equal access costs by the percent growth in their local switching revenues from the date LECs made their first annual access price cap filing through June 30, 1997. AT&T states that this adjustment would result in complete removal of such equal access costs from LECs' current traffic sensitive basket PCIs because this adjustment accounts for demand and price changes since their first annual access price cap filings.[63]

40. Most LECs argue that the *Access Charge Reform Order* did not explicitly require that the exogenous cost adjustment take into account the change in revenue growth and that they should, therefore, not be required to make this adjustment. Citing the *1995 Annual Access Order* as an analogy, LECs argue that the Commission cannot "after the fact" require LECs to take the change in revenue growth into account when calculating the equal access exogenous decrease. In the *1995 Annual Access Order*, the Common Carrier Bureau (Bureau) did not require OPEB adjustments to take account of any revenue adjustments. AT&T points out that the Bureau, in its Annual Access Tariff Filings of Price Cap Carriers, has required the LECs to utilize a revenue true-up procedure for adjustment of previous periods' exogenous cost sharing obligations. MCI argues that there is no logical difference between an exogenous adjustment of a sharing obligation from a LEC's PCI and the reversal of any other PCI adjustment. LECs respond that sharing is distinctly different from the reversal of equal access expense, because sharing involves the return of excess revenues through a price cap reduction. NYNEX challenges the revenue adjustment recommended by AT&T and used by Aliant. According to NYNEX, because the equal access rate was applied on a flat rate per-presubscribed line per month basis, the equal access revenues grew as a function of line growth, and not as a function of per-minute growth.

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[62] AT&T Petition at 10. AT&T states that, alone among the price cap LECs, Aliant has made the "R" value true up calculation properly. *Id.* at 11 n.12.

[63] AT&T Petition at 11-13.

41. We tentatively conclude that a revenue adjustment to the amortized equal access expenses, as opposed to a PCI adjustment, is a reasonable method of fully removing the amortized equal access costs from current rates. A revenue adjustment is reasonable in this case because it recognizes that price cap indices are adjusted to reflect the average basket price and a component of that price reflects equal access amortization. It further recognizes that as demand has grown over time, the revenue recovered through this equal access amortization component of price has grown correspondingly. Therefore, to remove fully the revenues being collected today associated with the amortized equal access cost, we tentatively conclude that the LECs must account for this demand growth.

42. We seek comment on the "R" adjustment used by Aliant and proposed by AT&T, particularly their use of growth rates in LECs' local switching revenue growth rates to calculate the exogenous cost adjustment. We also seek comment on whether an "R" adjustment related to the reversal of the equal access expense is or is not similar to reversal of sharing obligations. In addition, we invite parties to submit alternative proposals for measuring the downward exogenous cost true-up adjustment that LECs are required to make to account for the completion of the amortization of equal access non-capitalized expenses. Commenters must fully justify their proposals. Commenters may also address whether the Commission should prescribe the particular methodology for removing these costs or whether the Commission should allow LECs to use any reasonable method that completely removes the amortized equal access expenses from their rates.

43. We direct Ameritech, Bell Atlantic, BellSouth, Frontier, GTE, Aliant, Nevada Bell, NYNEX, Pacific Bell, Rochester, SNET, Southwestern Bell, and U S West to submit data on the local switching revenue of their traffic sensitive basket as reflected in their initial price cap filings. These data will allow the Commission to calculate the revenue change for each of these companies from the dates they made their initial price cap filings through June 30, 1997.

44. Calculation of the Initial Equal Access Exogenous Cost Revenue Requirement. In calculating its initial equal access exogenous cost revenue requirement, SNET is the only price cap LEC that included equal access expenses from prior periods, but not from the 1990 period. AT&T asserts that, based on the data in the 1990 Cost of Service No. 5 Report (COS-5), SNET underestimated its equal access exogenous cost adjustment by approximately $2.1 million. SNET responds that it accurately estimated its equal access exogenous cost adjustment because the Commission's instructions for completing the 1990 annual access tariff filings required LECs to include equal access expense from prior periods, but not from the "current" period, which at that time was the 1990 period. We require SNET to identify the specific part of the instructions for completing the 1990 annual access tariff filings that permitted SNET to include equal access expenses from prior periods, but not from the 1990 period. We also seek comment from SNET and other parties as to how SNET's adjustment should be treated in calculating the exogenous cost reduction required in the *Access Charge Reform Order*.

45. AT&T also claims that Ameritech failed to compute properly the proportion of equal access amortization revenue requirements associated with the total equal access revenue requirements because Ameritech did not use data contained in the 1990 COS-5 Report. Ameritech argues that it used "separations information system" materials to determine the portion of the equal access costs that were amortized because the COS-5 Report only reveals total equal access costs. We seek comment on whether Ameritech was able to calculate accurately the equal access amortization revenue requirement through the use of internal separations data. We require Ameritech to explain and document fully how it used its separations information system data to determine the portion of the equal access costs that was amortized. In particular, Ameritech must fully explain and document the data, assumptions, and methodologies that were used to calculate the equal access costs that were amortized. These explanations must include a copy of all studies that were conducted to calculate equal access costs that were amortized.

C. Other Billing and Collection Exogenous Cost Increases

1. Background

46. Earlier this year, the Commission changed the separations rules applicable to Other Billing and Collection (OB&C) Expense.[64] Effective May 1, 1997, the *OB&C Order* revised these rules to replace a complicated allocation procedure relying on user and message counts with a simple allocation procedure based on a fixed allocator of 33% or 5%, depending on whether the price cap LEC performs any end user billing for IXCs.[65] Price cap LECs were required to file exogenous adjustments to reflect these changes in the separations rules.[66]

47. In the *Suspension Order*, we found that U S WEST's OB&C exogenous adjustment of $845,145, which U S WEST claimed was necessary in order to recover the two months of OB&C costs between May 1 and July 1, 1997, raises substantial questions of lawfulness.[67] Further, we were not persuaded that other aspects of its treatment of OB&C Expense are lawful. In particular, we noted that U S West's ARMIS Report 43-04 shows that its allocation factors (i.e., the relative usage measurements it is required to use as a basis for allocating OB&C Expense among service categories and between the intrastate and interstate jurisdictions) are inconsistent with its allocation of that expense.

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[64] Amendment of Part 36 of The Commission's Rules and Establishment of a Joint Board, FCC 97-30, Rel. February 3, 1997.

[65] *Id.* at ¶¶ 13-17.

[66] 47 C.F.R. §§ 61.45(d)(1)(iii), 61.44(c).

[67] *1997 Annual Access Suspension Order* at ¶¶ 47-48, 51.

48. In addition, we stated that GTE has not adequately explained why it accounts for more than half of the total OB&C exogenous cost amounts claimed by all LECs in the April filings. We found that this anomaly raises substantial questions of lawfulness.[68]

49. We also found a disparity between the portion of billing revenues that Pacific Bell allocated to the interstate jurisdiction and the portion of billed toll messages that it attributed to interstate services. We noted that Pacific Bell's data submission shows that the share of these toll messages attributed to interstate calls declined by more than 66 percent between the end of calendar year 1994 and the end of calendar year 1995 even though its corresponding interstate revenues (from billing and collection services provided to IXCs) increased slightly during that same year. We stated that Pacific Bell has not explained how such a precipitous decline in billed interstate messages could have occurred at a time when the associated revenues were increasing. In addition, we found that Pacific Bell may have overstated its exogenous cost changes by using the wrong base period. While most other price cap LECs used 1996 data when calculating such changes,[69] Pacific Bell used 1995 data. We believe that if Pacific Bell had used 1996 data, its calculated exogenous changes would have still been substantial because its 1996 interstate assignment of OB&C Expense was far below the 33 percent interstate assignment prescribed by the new separations rule. Pacific Bell's interstate assignment in 1995, however, was even lower than its interstate assignment in 1996. Hence, by using 1995 data, rather than 1996 data, Pacific Bell's calculations showed that the new rule had a greater impact when raising its interstate assignment to the 33 percent level. Because Pacific Bell has not explained its use of 1995 base period data or the discrepancies discussed above, we found that its tariff raises a substantial question of lawfulness.[70]

2. <u>Information Requirements and Issues Designated for Investigation</u>

50. The data disparities and anomalies identified above, which are discussed in greater detail below, raise questions as to whether GTE, Pacific Bell, and U S West are in compliance with the Commission's jurisdictional separations rules for OB&C Expense and have properly calculated the exogenous change resulting from the 1997 change to those rules. We therefore require these companies to explain and document the process by which they separate OB&C Expense between the intrastate and interstate jurisdictions. To facilitate our analysis of that process, we also require these companies to explain and document the process by which they separate the corresponding revenues, Carrier Billing and Collection Revenues. Although the jurisdictional separations of those revenues did not affect the companies' claimed exogenous changes because those revenues are non-regulated, we intend to use the

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[68] *Id.* at ¶ 52.

[69] *See Infra* Para. 58. GTE used 12 months ended June 1996 for purposes of calculating its exogenous change.

[70] *Id.* at ¶ 53.

associated jurisdictional allocation factors, *i.e.*, the message counts used for separating such revenues, as a basis for evaluating the message counts used for separating the message toll portion of OB&C Expense. This evaluation procedure seems reasonable given that the companies apparently used message counts as a basis for separating both revenues and expenses.

51. Further, because calculation of an exogenous change requires a comparison of separations procedures used in 1990 (the base year for initializing price caps) with separations procedures used in 1996 (the base year for the 1997 annual access charge filings), we require the companies to explain and document in response to the data requirements outlined below, the procedures they used for computing their separated interstate OB&C Expense for calendar years 1990 and 1996. Moreover, we require them to explain and document this process for the intervening years, 1991 through 1995, to provide a basis for evaluating the reasonableness of their transition from 1990 procedures to 1996 procedures. Accordingly, GTE, Pacific Bell, and U S West shall provide, for the calendar years 1990 through 1996, the information required below on both a holding company level and COSA level.

(a) Provide the user counts that were used as a basis for allocating OB&C Expense among the service categories prescribed by Section 36.380(b) of the Commission's rules. Show these counts for the following service categories: message toll telephone, exchange including semi-public, directory advertising, and private line.

(b) Explain the process by which users were counted for jurisdictional separations purposes during this seven-year period. In particular, explain the assumptions (including the time period over which information was gathered) and methodologies that were used.

(c) Identify any discrepancies that exist between the user counts provided in response to (a) above and those that were reported in ARMIS Report 43-04. These LECs must explain why these discrepancies occurred.[71] Similarly, they must identify and explain any discrepancies that exist between the 1990 user counts provided in response to (a) above and those that were used to calculate interstate costs when they converted from cost of service to price cap regulation.

(d) Provide the message counts used in allocating the message toll portion of OB&C Expense between the intrastate and interstate jurisdictions.

(e) Explain the process by which messages were counted for jurisdictional separations purposes during this seven-year period. In particular, explain the

[71] If the companies find any data that has been incorrectly reported in ARMIS for the period 1990 through 1996, they should refile the ARMIS data with the Commission.

assumptions (including the time period over which information was gathered) and methodologies that were used.

(f) In the event that the message counts provided in response to (d) exclude some toll messages that appear on customer bills, provide the counts for the excluded messages and explain why these message counts were not included in the allocation factor used for separating the message toll portion of OB&C Expense. Pacific Bell, for example, should provide message counts for the billed messages associated with its *invoice-ready* billing service and should explain why its allocation factor apparently includes only the billed messages associated with its *message-ready* billing service.[72]

(g) Identify any discrepancies that exist between the message counts provided in response to (d) and those that were reported in ARMIS Report 43-04. Explain why these discrepancies occurred. Similarly, identify and explain any discrepancies that exist between the 1990 message counts provided in response to (d) and those that were used to calculate interstate costs when initializing price caps.

(h) Explain and document how Carrier Billing and Collection Revenue was jurisdictionally separated during this period. If this revenue was separated based on toll message counts, identify these counts. In the event that such counts differ from the toll message counts discussed above, explain why. If an alternative methodology was used for separating these revenues, identify the measurements used as a basis of allocation.

(i) Explain any instances where OB&C Expense is not categorized or apportioned according to the prescribed factors and provide revised separations results reflecting appropriate use of the prescribed factors. U S WEST, for example, seems to have assigned directly a portion of its OB&C Expense to the intrastate jurisdiction prior to categorizing that expense. U S WEST should correct its separations results to reflect use of the prescribed allocation procedures, which do not permit use of direct assignment.[73]

52. Further, we require GTE, Pacific Bell, and U S WEST to provide the following additional information:

(a) If any message counts or user counts that are used as a basis of allocation remain constant from one year to the next, explain why. We are seeking this

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[72] Letter from Sheryl L. Herauf to William F. Caton, dated July 3, 1997, AAD 97-77, Pacific Bell Petition for Expedited Waiver of Section 36.380 of the Commission's Rules, filed July 2, 1997.

[73] 47 C.F.R. §36.380(b).

information because it appears that the companies may have used allocation factors that were updated too infrequently to reflect reasonably the relative use of the billing and collection function by different service classes. Pacific Bell, for example, should explain why, during calendar years 1994 through 1996, the interstate share of invoice-ready *billing service revenues* remained constant while the interstate share of related invoice-ready *toll message counts* varied substantially during that period.[74] This disparity seems unreasonable because Pacific Bell asserts that it separated the revenues from its invoice-ready billing services based on the associated message counts.[75]

(b) Provide work papers showing the calculations of the OB&C exogenous change contained in the 1997 Price Cap filing. GTE should calculate the exogenous change using calendar year 1996 data rather than the twelve months ended June 1996. If any errors in that calculation are discovered when responding to data requests in this order, provide a corrected calculation. We are seeking this information because it appears that these three companies may have miscalculated the exogenous change, either by incorrectly separating the OB&C Expense or by incorrectly apportioning that expense among the Part 69 access elements.

53. We require GTE to explain and document the methodology it used, during the period 1990 through 1996, to distribute customer services expense among the three categories prescribed by section 36.376 of the Commission's rules. In particular, we require GTE to explain why Category 3, All Other Customer Services Expense, grew rapidly during that period, increasing from 18 percent to 28 percent of total customer services expense.[76] GTE must also explain why Category 1, Business Office Expense, declined rapidly during that period, decreasing from 60 percent to 47 percent of total customer services expense.[77] We seek this information because these changes suggest that the 1996 Category 3 expense may mistakenly include a portion of business office expense that GTE had properly assigned to Category 1 in 1990. We observe that GTE's Category 3 assignment is unusually large when compared to that of the RBOCs. In 1996, the share of customer services expense that GTE assigned to Category 3 was more than double the largest share assigned by any RBOC during

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[74] Letter from B. Jeannie Fry to William F. Caton, dated July 9, 1997, AAD 97-77, Pacific Bell Petition for Expedited Waiver of Section 36.380 of the Commission's Rules, filed July 9, 1997. Pacific Bell requests that the data contained in the attachments to the Ex Parte filing be treated as confidential and proprietary.

[75] Letter from Sheryl L. Herauf to William F. Caton, dated July 3, 1997, AAD 97-77, Pacific Bell Petition for Expedited Waiver of Section 36.380 of the Commission's Rules, filed July 2, 1997.

[76] FCC ARMIS 43-04 Report (1990-96), Rows 7300 and 7310, for GTE Corporation.

[77] FCC ARMIS Report 43-04 (1990-96), Rows 7220 and 7310, for GTE Corporation.